



COMMONWEALTH OF PENNSYLVANIA  
PENNSYLVANIA PUBLIC UTILITY COMMISSION  
P.O. BOX 3265, HARRISBURG, PA 17105-3265

IN REPLY PLEASE  
REFER TO OUR FILE

November 1, 2010

Rosemary Chiavetta, Secretary  
Pennsylvania Public Utility Commission  
PO Box 3265  
Harrisburg, PA 17105-3265

Re: Pennsylvania Public Utility Commission v.  
Petition of West Penn Power Company d/b/a Allegheny Power for  
Expedited Approval of its Smart meter Technology Procurement and  
Installation Plan

Docket No. M-2009-2123951

Dear Secretary Chiavetta:

Enclosed please find an original and ten (10) copies of the Office of Trial Staff's  
(OTS) **Answer** in the above-captioned proceeding.

Copies are being served on all active parties of record.

Sincerely,

Richard A. Kanaskie  
Senior Prosecutor  
Office of Trial Staff  
PA Attorney I.D. #80409

RAK/slc

cc: Parties of record  
Honorable Mark A. Hoyer  
Chairman Cawley  
Vice Chairman Christy  
Commissioner Coleman  
Commissioner Gardner  
Commissioner Powelson  
Chief Counsel Pankiw  
Director Davis

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PA PUBLIC UTILITY COMMISSION  
SECRETARY'S BUREAU

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Petition of West Penn Power Company :  
d/b/a Allegheny Power for Expedited : Docket No. M-2009-2123951  
Approval of its Smart Meter Technology :  
Procurement and Installation Plan :**

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SECRETARY'S BUREAU

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**ANSWER OF THE  
OFFICE OF TRIAL STAFF IN  
OPPOSITION TO THE  
JOINT PETITION FOR SETTLEMENT**

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On October 19, 2010, West Penn Power Company d/b/a Allegheny Power (“West Penn” or “Company”) and the Office of Consumer Advocate (“OCA”) (collectively, “Joint Signatories”) filed a document with the Pennsylvania Public Utility Commission (“Commission”) entitled *Joint Petition For Settlement* (“Settlement” or “Joint Petition”). The Office of Trial Staff (“OTS”) maintains that the filed document merely represents an agreement between the Joint Signatories purportedly resolving their respective issues in the above referenced proceeding. It does not contain any representations from the Office of Trial Staff nor does it satisfy the issues raised throughout this proceeding. The document appears to be nothing more than a Stipulation between the Company and OCA that was subsequently styled as a Joint Petition to satisfy the Commission’s Order Entered July 21, 2010.<sup>1</sup> The Commission’s Order required the submission of a proposed

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<sup>1</sup> *In Re: Petition of West Penn Power Company d/b/a Allegheny Power for Expedited Approval of its Smart Meter Technology and Installation Plan*, Docket No. M-2009-2123951, Opinion and Order Adopted July 15, 2010 and Entered July 21, 2010.

settlement within 90 days.<sup>2</sup> In the alternative, the Order established the Exception and Reply Exception period to address Administrative Law Judge Hoyer's Initial Decision issued May 6, 2010.<sup>3</sup> The representation of the Joint Signatories' submission as a Joint Petition for Settlement is both procedurally flawed<sup>4</sup> and substantively insufficient. As such, it fails to satisfy the requirements of the Commission's July 21, 2010 Order.<sup>5</sup> Furthermore, the proposed agreement between the Company and the OCA fails to satisfy the legal standard for approval of a settlement and must be rejected. Any consideration of the terms contained in the agreement between the Joint Signatories must be supported by substantial evidence. Having failed this requirement, rejection is necessary. In the alternative, a new procedural schedule must be developed to allow for the presentation of evidence.

The Office of Trial Staff is charged with representing the public interest in Commission proceedings having an impact on customer rates. The OTS representation of the public interest includes balancing the interests of ratepayers, utilities and the

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2 Id. p. 12.

3 Id. The Commission's Order indicated that Exceptions to the Initial Decision will be due one hundred and ten (110) days after the entry date of this Opinion and Order with Reply Exceptions due one hundred and twenty (120) days after entry of the Opinion and Order.

4 52 Pa. Code § 5.232(b) states that "[a] settlement agreement must specifically identify the parties: (1) Supporting the settlement. (2) Opposing the settlement. (3) Taking no position on the settlement. (4) Denied an opportunity to enter into the settlement. The Office of Trial Staff articulated its opposition to the proposed settlement when initially presented the document by the Company. In addition, the Office of Small Business Advocate has expressed its opposition. The only public advocate joining as a signatory is the Office of Consumer Advocate.

5 The Commission's Order Adopted on July 15, 2010 and Entered on July 21, 2010 at Docket No. M-2009-2123951 on page 11 stated that "[i]f West Penn and the Parties have not filed a proposed Settlement Agreement in this matter...by ninety (90) days from the date of entry of this Opinion and Order, then Exceptions to the Initial Decision will be due one hundred and ten (110) days after the entry date of this Opinion and Order with Reply Exceptions due one hundred and twenty (120) days after the entry date of this Opinion and Order." West Penn and only one party have submitted any type of agreement. OTS interprets the Commission's Order and Opinion as anticipating a comprehensive settlement among all the parties. A singular agreement with one party does not satisfy the Commission Order and Opinion.

welfare of the Commonwealth. OTS initially filed its Notice of Appearance in this proceeding on August 20, 2009 in order to carry out its charge because West Penn's Smart Meter Implementation Plan involves significant costs and includes a flawed recovery mechanism designed to recoup those costs solely from its ratepayers. As such, OTS has examined the Company's Plan with an emphasis on cost recovery proposal and the subsequent ratemaking impact of the proposed programs. OTS has remained active in this proceeding and continues to concentrate its evaluation on the Company's proposed cost recovery mechanism including alternatives presented in the agreement between the Joint Signatories.

Pursuant to 52 Pa. Code § 5.61,<sup>6</sup> the Office of Trial Staff hereby files these timely Comments in Opposition to the Joint Petition for Settlement offered by the Company and the Office of Consumer Advocate. OTS requests that the Commission assign this Petition to the Office of Administrative Law Judge ("OALJ") for a thorough investigation and the development of a complete record. OTS maintains that there are issues of fact and law requiring clarification. As such, the Petition is deficient and should not be approved in its present form. In support of this Answer OTS offers the following enumerated responses to the agreement between the Joint Signatories:

## **I. BACKGROUND AND PROCEDURAL HISTORY**

1. Admitted.

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<sup>6</sup> The pertinent section provides that answers to complaints and petitions shall be filed with the Commission within 20 days after the date of service. This provision has been changed by the Secretary's granting of an expedited period to submit Answers. The granting of the expedited period for responses occurred before any party was given an opportunity to address that request.

2. Admitted in part. The procedural history as presented is admitted. The provisions of Act 129 speak for themselves and any averments pertaining to its interpretation are denied.

3. Admitted in part. It is admitted that the Company filed its Smart Meter Implementation Plan on August 14, 2009. The provisions of Act 129 speak for themselves and any averments pertaining to its interpretation are denied. OTS is without sufficient knowledge or information to form an opinion as to the intent of the Company's Smart Meter Implementation Plan.

4. Admitted.

5. Admitted. Administrative Law Judge Mark A. Hoyer presided.

6. Admitted.

7. Admitted.

8. Admitted.

9. Admitted. Administrative Law Judge Hoyer's Initial Decision is dated April 29, 2010. The Initial Decision was subsequently issued on May 6, 2010.

10. Admitted in part. It is admitted that the Company filed a Petition to Stay the Exceptions Period on May 13, 2010. By way of further comment, OTS is without sufficient knowledge or information to form an opinion as to whether the sole basis for the filing was "so that the parties may consider the impact on Allegheny Power's proposed SMIP given the proposed merger of Allegheny Power's parent company..."

11. Denied to the extent the averment attempts to interpret the Commission's Secretarial Letter. The referenced documents speak for themselves and no response is necessary.

12. The Commission's Opinion and Order Adopted July 15, 2010 and Entered July 21, 2010 speaks for itself and no response is necessary.

13. Admitted.

## **II. SETTLEMENT**

14. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. By way of further comment, OTS is without sufficient knowledge or information to form an opinion as to whether "[a]dopting a less rapid smart meter deployment schedule together with the Amended EE&C/DR Plan...will allow Allegheny Power and its Pennsylvania customers to avoid certain near term expenditures, as well as provide time for analysis of whether a less costly smart meter deployment can be designed." It is denied that there is substantial evidence in the record to support that this provision is in the public interest.

15. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. It is denied that there is substantial evidence in the record to support that this provision is in the public interest.

16. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. By way of further comment, OTS is without sufficient knowledge or information to form an opinion

as to efficacy of severing altering its approved EE&C/DR Plan to deploy only 25,000 meters based on customer requests. It is denied that there is substantial evidence in the record to support that this provision is in the public interest.

17. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS questions the impact of failing to provide In Home Devices to support installed Smart Meters. There is not sufficient record evidence to support how a Smart Meter will benefit a ratepayer without an In Home Display. It is denied that there is substantial evidence in the record to support that this provision is in the public interest.

18. OTS is without sufficient knowledge or information to form a belief as to the accuracy of the averments contained in this paragraph as they represent an agreement only between the Company and the Office of Consumer Advocate. To the extent the averments are unsupported, OTS denies the representations. OTS maintains that there is insufficient evidence in the Joint Petition to support the claims contained therein. Appendix "A" referenced in this averment provides no detail as to the claimed expenses and fails to satisfy the legal standard of substantial evidence. Furthermore, the agreement between the Company and OCA claims an interest rate on deferred amounts to the detriment of ratepayers. OTS denies that the inclusion of this provision is in the public interest and requests the matter be remanded to the presiding officer for the scheduling of Hearings to adjudicate this matter. The amount of interest that ratepayers will bear has not been established and the legal support for providing this benefit to the Company is lacking.

19. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. To the extent the averments are offered in support of the proposed agreement, OTS denies the representations. OTS maintains that there is insufficient evidence in the Joint Petition to support the claims contained therein. Appendix "A" referenced in this averment provides no detail as to the claimed expenses and fails to satisfy the legal standard of substantial evidence. Furthermore, the settlement between the Company and OCA claims an interest rate on deferred amounts to the detriment of ratepayers. OTS denies that the inclusion of this provision is in the public interest and requests the matter be remanded to the presiding officer for the scheduling of Hearings to adjudicate this matter.

20. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. Notwithstanding the offering in this averment, OTS retains all applicable rights in this proceeding.

21. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. Notwithstanding the offering in this averment, OTS retains all applicable rights in this proceeding.

22. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. By way of further comment, OTS is without sufficient knowledge or information to form an opinion as to the validity of the representations in this averment.

23. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required.

24. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. Barring the submission of additional evidence, OTS denies that this averment is in the public interest. OTS recommends that Commission staff calculate a cost rate of common equity for the electric industry and present it in the Quarterly Earnings Report.<sup>7</sup> This cost rate of common equity will be based on the Commission's barometer group, which will be used to determine the appropriate capital structure discussed above. Until the next Quarterly Earnings Report establishes the capital structure for smart meter cost recovery, OTS recommends that the capital structure be published in the Order in this proceeding.<sup>8</sup>

The OTS recommendation that the Commission calculate the cost rate of common equity and capital structure based on its barometer group is appropriate because it properly matches the financial risk associated with the capital structure to the cost rate of common equity.<sup>9</sup> Additionally, applying a Commission calculated cost rate of common equity is an established Commission procedure that has been used in DSIC proceedings for the water industry. In DSIC proceedings, the individual equity returns for the water utilities are not used. Instead, the Commission calculates a cost rate of common equity that is then applied to all companies utilizing a DSIC mechanism to recover the appropriate costs. The OTS recommendation is to apply this same principle to smart

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7 OTS St. No. 1, p. 14.

8 OTS St. No. 1, p. 15.

9 Id.

meter cost recovery. The appropriate comparison is that the mechanism applies to the recovery of capital additions prior to incorporation in base rates. The Commission's Bureau of Fixed Utility Services currently calculates a market indicated common equity cost range for the electric company barometer group in the Quarterly Earnings reports.<sup>10</sup> Therefore, this procedure can be applied to smart meter costs.

The rate of return is calculated by determining the proportions of capital and assigning a cost rate to each type of capital. Therefore, it is first necessary to determine the capital structure, which is the proportion of long term debt, preferred stock and common equity.<sup>11</sup> OTS recommends that the Commission use a representative capital structure for all EDCs in the recovery of smart meter costs that is based upon the barometer group in the Quarterly Earnings Report.<sup>12</sup> As such, the Commission would calculate the appropriate capital structure and publish it in the Quarterly Earnings Report. Until the next Quarterly Earnings Report establishes the capital structure for smart meter cost recovery, OTS recommends that the capital structure be published in the Order in this proceeding.<sup>13</sup>

The representative capital structure is important for two reasons. First, as will be discussed in greater detail below, the representative capital structure is based on the same barometer group that will be used to determine the appropriate cost rate of common equity. Therefore, under the OTS recommendation, the representative capital structure will properly match the financial risk associated with the corresponding cost rate of

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10 OTS St. No. 1, p. 14.

11 OTS St. No. 1, p. 11.

12 OTS St. No. 1, p. 15.

13 OTS St. No. 1-R, pp. 4-5.

common equity.<sup>14</sup> Second, OTS is recommending a representative capital structure for all EDCs, which is important because some electric companies have capital structures that are not representative of the industry norm.<sup>15</sup> As such, using a uniform representative capital structure will not advantage or disadvantage any EDC or its ratepayers. OTS recognizes that implementing a representative capital structure deviates from what is currently used in DSIC proceedings; however, capital structures of water companies are more closely aligned with the industry norm.<sup>16</sup> Such is not the case in the electric industry, making the OTS recommendation appropriate for smart meter cost recovery. Accordingly, the OTS recommendation provides for a capital structure that is representative of the electric industry and should be approved by the Commission.

With regard to the cost rate of debt and preferred stock, OTS recommends that the Company's actual costs, as found in the most recent quarterly Financial Report,<sup>17</sup> be used in establishing the appropriate costs for this component of the revenue requirement. The cost rate of preferred stock should be blended with the cost rate of debt to determine a composite cost rate for the fixed rate portion of the capital structure. This recommendation is appropriate because it reflects the Company's current cost rate and will best reflect the cost of capital used to finance the smart meter technology.

25. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. By way of

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14 OTS St. No. 1, p. 15.

15 Id.

16 OTS St. No. 1-R, p. 6. OTS Ex. No. 1-R, pp. 1-2.

17 OTS St. No. 1, p. 16.

further comment, OTS is without sufficient knowledge or information to form an opinion as to goal of this averment.

26. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required.

27. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required.

28. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required.

29. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required.

Notwithstanding the offering in this averment, OTS retains all applicable rights in this proceeding.

30. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

31. Any representations as to the Commission approved EE&C/DR Plan are denied. The Commission approved EE&C/DR Plan speaks for itself and no interpretations are warranted in this Petition. Notwithstanding the offering in this averment, OTS retains all applicable rights in this proceeding.

32. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS

denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

### **III. THE SETTLEMENT IS NOT IN THE PUBLIC INTEREST**

33. Denied. The proposed agreement between the Company and OCA is not lawful as it lacks substantial evidence to support the averments contained therein. OTS is without sufficient knowledge or information to offer any comment as to how the Company and the OCA arrived at their agreement. It is denied that the referenced direct and rebuttal testimonies satisfy the standard of substantial evidence in support of this agreement.

34. Admitted. The submitted Joint Petition contains the referenced documents. By way of further comment, OTS disagrees with the opinions presented in the accompanying documents as they fail to establish that the Joint Petition is in the public interest. The Statements in Support lack evidentiary value as they have not been presented as evidence or defended before the Administrative Law Judge and the intervening parties.

### **IV. CONDITIONS OF SETTLEMENT**

35. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

36. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS

denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

37. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

38. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

39. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

40. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest.

41. To the extent this averment describes the terms of OCA and the Company's Stipulation, it represents a Prayer for Relief to which no response is required. OTS denies that this provision supports any representation that the agreement between the Company and OCA is in the public interest. By way of further comment, the averment's

reference to compromise represents an agreement only between the Company and the OCA.

42. Admitted. Counsel for OTS received an electronic copy of the document entitled *Joint Petition for Settlement* on October 19, 2010 at 4:06 p.m.

43. Admitted in part, denied in part. It is admitted that a document purported to be a Joint Petition for Settlement is not unanimous. In fact, the Joint Petition merely represents a Stipulation between only the Company and the OCA. The requested terms and provisions have no force or impact on the non-signatory parties. Although a moot point, the request for an expedited Answer period should have been rejected or, at a minimum, parties should have been afforded an opportunity to respond. The following sequence of events illustrates that the Secretary granted the request for expedited review in this contested proceeding without providing the parties adequate time to address this proposal. OTS received an electronic copy of the agreement between the Company and OCA on Tuesday, October 19, 2010 at 4:06 p.m. A Secretarial letter granting the shortening of the response period was issued on Thursday, October 21, 2010. OTS received notification of the Secretary's granting of the expedited Answer period on Monday, October 25, 2010.<sup>18</sup> Given that the Secretary of the Commission granted the request in two days, the ability of the parties to address the requested expedited time period for providing Answers was unilaterally negated. The document entitled Joint Petition for Settlement indicated that it was not a unanimous agreement. This should have been indicative of a contested proceeding and adequate time should have been

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<sup>18</sup> The Secretarial Letter was time stamped in OTS at 2:33 p.m.

allowed for responses. Furthermore, the Secretarial Letter improperly states that “the potential contested issues have been reduced.” This representation is incorrect as only two (2) parties have come to any sort of agreement. In fact, the Commission’s Order and Opinion has acknowledged “the relative complexity of the issues involved.”<sup>19</sup>

Furthermore, the Secretarial Letter’s acknowledgment of West Penn’s averment that OCA was the party that most intensely litigated this proceeding is both inaccurate and inconsequential. This baseless statement must be ignored as it seemingly is offered as some support that an agreement between the Company and the Office of Consumer Advocate is all that is necessary to adjudicate a matter. Accordingly, OTS objects to the granting of the expedited period for Answers to the filing as it severely limited the rights of the intervening parties.

In conclusion, OTS offers a summary of its positions presented throughout this proceeding. OTS has not challenged the programs or proposals that West Penn considers integral to the success of its Smart Meter Plan. Rather, OTS maintains that the Company’s proposed Cost Recovery Mechanism requires modification to ensure adequate protection to ratepayers while enabling the Company to recover all of the appropriate costs associated with the implementation of its Plan.

It is not disputed that Act 129 permits electric distribution companies (“EDC”) to recover the reasonable and prudent cost of implementing smart meter technology either

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<sup>19</sup> Docket No. M-2009-2123951, Opinion and Order Adopted July 15, 2010, Entered July 21, 2010, p. 11.

through base rates or through a reconcilable automatic adjustment clause under Section 1307 of the Public Utility Code.<sup>20</sup>

While the Act and the subsequent Implementation Order primarily provide guidance as to the contents of the Smart Meter Plans, OTS reaffirms the following recommendations with regard to the appropriate procedure for smart meter technology cost recovery that have been presented in its filings throughout this proceeding. First, the need for annual review and reconciliation is well established; however, in addition OTS continues its recommendation that West Penn be required to file quarterly adjustments to the rates in its surcharge upon approval of its Smart Meter Plan. West Penn has stated that its proposal contains a mechanism allowing it to recover the actual costs of implementing the proposed program. OTS maintains that revenue rate adjustments done on a quarterly basis will assist the Company in attaining its goal by allowing it to update projected revenue on a timely basis in order to more accurately match planned costs. Additionally, the quarterly adjustments will minimize dramatic fluctuations in the reconciliation of costs and revenue to be done in its annual filing thereby offering protections to both the Company and its ratepayers.

The second OTS recommendation is that the Commission adopt a procedural schedule to review and reconcile costs incurred in West Penn's Smart Meter Plan. The Implementation Order states that the tariff mechanism will be subject to annual review and reconciliation in accordance with 66 Pa. C.S.A. § 1307(e) and that such review and reconciliation will be scheduled to coincide with the submission of the "Smart Meter

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<sup>20</sup> 66 Pa.C.S.A. § 2807(f)(7)(ii).

Progress” annual report.<sup>21</sup> However, the Implementation Order does not provide a corresponding procedural schedule. OTS maintains that establishment of an annual procedural schedule is appropriate in this proceeding and further recommends that this schedule should require that West Penn’s annual filing be based on a fiscal year ending June 30. Based on the establishment of this fiscal year period, the following procedural schedule is recommended by OTS:

- 1) The Company’s annual filing is due on or before August 1, with the first filing occurring on or before August 1, 2011;
- 2) Evidentiary Hearings are to be held annually on or before October 1;
- 3) The Commission’s Order will be due on or before December 1 with an effective date of January 1.

OTS has recommended this procedural schedule to all EDCs in their respective filings as it will promote and maintain administrative and judicial efficiency in the review of these programs. Additionally, the proposed filing dates will not conflict with the annual 1307(f)<sup>22</sup> proceedings that currently are scheduled beginning in February (with Pre-filings in January) and continuing through July. Also, the proposed procedural schedule will avoid conflict with the annual filing of the EDCs Energy Efficiency and Conservation plans. Staggering the Smart Meter filings with the other annual proceedings will allow the parties and Commission sufficient time to review and analyze costs incurred to provide smart meter technology to West Penn’s customers.

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21 Implementation Order, p. 31.

22 66 Pa. C.S.A. § 1307(f).

In addition to the procedural recommendations provided above, OTS has also made specific recommendations concerning the mechanics of West Penn's proposed recovery of the costs associated with its Smart Meter Plan. While, as previously noted, West Penn seeks to recover the costs of its Smart Meter Plan through a reconcilable automatic adjustment clause as provided for in Section 1307 of the Public Utility Code; the Company has not included an interest component for over and under-collections in its cost recovery mechanism. Prudent regulation includes an interest component in mechanisms where over and under-collections occur in the course of cost recovery. OTS recommends that the Company's cost recovery mechanism must provide adequate protection to ratepayers. To accomplish this, OTS recommends the inclusion of the computation of interest to over and under-collections.

OTS recommends that the appropriate rate of interest to be computed on over and under-collections must be based on the Residential Mortgage Rate. This measure of interest provides the most accurate representation of the current cost of borrowed funds. Any net interest due to the Company resulting from the cumulative twelve month reconciliation period will not be recovered from ratepayers. No recovery of interest due to the Company is proper because West Penn will be permitted to recover capital costs associated with the deployment of its smart meter technology. This return component compensates West Penn for the lost time value of money and the Company, therefore, should not assess interest to its under-collections. Receiving interest on under-collections and earning a return of financed capital assets violates the tenets of sound regulation.

OTS has presented testimony addressing the methodology that must be established to calculate the appropriate return component associated with the planned capital assets. As discussed earlier, Act 129 allows for the recovery of the reasonable and prudent costs of providing smart meter technology.<sup>23</sup> Furthermore, these costs are to be offset by any operating and capital cost savings resulting from the implementation and subsequent use of Smart Meter equipment and technology.<sup>24</sup> The implementation of the Company's Smart Meter Program in this proceeding will involve both operating expenses and capital costs. The costs of prudent operating expenses and appropriate capital expenditures are recovered by the Company in different ways. Prudent operating expenses are recoverable on a dollar for dollar basis under all generally accepted ratemaking formulas. The proper regulatory treatment of the capital additions made by the Company in accordance with the mandates of Act 129 is to treat them as if in rate base where they will earn a fair rate of return. OTS has confirmed in its testimony that an overwhelming majority of the costs associated with the implementation of the Company's Smart Meter Program will be capital costs. As such, the cost of these capital expenditures will be returned to the Company through depreciation and the applicable Rate of Return component.

“An EDC may recover smart meter technology costs through (1) base rates,...or (2) on a full and current basis through a reconcilable automatic adjustment clause under Section 1307.”<sup>25</sup> With either recovery mechanism, a rate of return component is applicable to ensure that the Company recovers the costs associated with its capital

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23 Implementation Order, p. 28.

24 Id.

25 Id., citing 66 Pa. C.S.A. § 2807(f)(7).

additions. Rate base treatment is well documented under the Commission's Regulations and there is significant Commission precedent defining the appropriate procedures. In addition, guidance on the applicable rate of return component in automatic adjustment clauses can be found in the Commission's review of surcharges associated with the Distribution System Improvement Charge ("DSIC").

As presented above, OTS maintains that the appropriate calculation and determination of the cost to be applied to the return on equity component contained in the proposed automatic adjustment clause should be calculated by the Commission and presented in the Quarterly Earnings Report. The effect of this measure will be to provide for the timely recovery of the capital costs to implement this project. In addition, the return on equity calculated by the Commission on a quarterly basis will place all EDCs on somewhat equal grounds.

In order to determine an equitable capital structure, OTS recommends that the average of the capital structures of the proxy companies presented in the Commission's Quarterly Earnings Report serve as the basis for the capital structure to be applied to the rate of return component in this proceeding. As such, the capital structure ratios will be based on the same proxy companies that are used to determine the cost of equity thereby assuring the proper matching of risk and return. The data for the determination of the applicable ratios will be readily available in the quarterly earnings reports and will result in current information.

Individual company data to be used in the Rate of Return determination will consist of the ongoing debt cost as contained in the Company Quarterly Financial

Reports. OTS opines that these calculations are better reflected through the use of the actual figures presented by each company. The use of actual numbers for debt and preferred equity on a quarterly basis will be the most accurate measure of these components in the Rate of Return calculation.

The rate of return component associated with the Company's capital expenditures is based on the weighted cost of capital. The weighted cost of capital results from the Company's capital structure and the relationship to the financing sources providing the associated capital. Financing sources typically consists of debt, preferred stock and common equity. As each of these financing vehicles has a different cost rate, the weighted cost of capital accounts for the variances in quantity of financing by instrument as well as differing cost.

OTS recommends that the Commission calculate the applicable rate of return to be used in an automatic adjustment clause on a quarterly basis. This determination should be based on an industry calculated return on equity and capital structure in conjunction with individual company debt and preferred equity costs. In this proceeding, OTS recognizes that West Penn's most recent capital structure does not include preferred stock. These measures will provide equal treatment for each EDC while providing for a recovery of capital costs based on current criteria.

**WHEREFORE**, The Office of Trial Staff specifically requests that the agreement between West Penn Power Company d/b/a Allegheny Power and the Office of Consumer Advocate be rejected as it is unsupported by any credible evidence. In the alternative, the Office of Trial Staff requests that Evidentiary Hearings be scheduled allowing for the development of a full and complete record on the substance of the proposed agreement between West Penn Power Company d/b/a Allegheny Power and the Office of Consumer Advocate. OTS opposes the request for expediting the hearing and associated procedural steps as this request impedes the development of a full and complete record. There is simply no credible reason to continue to request expedited review as it negatively impacts the development of a record to support the disposition of this proceeding. As the proposed agreement between the Company and OCA impacts the Company's Smart Meter Implementation Plan and its previously approved EE&C/DR Plan, sufficient time must be devoted to the regulatory review of this proposal.



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Dated: November 1, 2010

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of West Penn Power Company :  
d/b/a Allegheny Power for Expedited : Docket No. M-2009-2123951  
Approval of its Smart meter Technology :  
Procurement and Installation Plan :

**CERTIFICATE OF SERVICE**

I hereby certify that I am serving the foregoing **Comments** dated November 1, 2010, either personally, by first class mail, electronic mail, express mail and/or by fax upon the persons listed below, in accordance with the requirements of § 1.54 (relating to service by a party):

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